DIRECT TESTIMONY

OF

CARLETTE L. WALKER

ON BEHALF OF

SOUTH CAROLINA ELECTRIC & GAS COMPANY

DOCKET NO. 2004-178-E

Q. PLEASE STATE YOUR FULL NAME AND BUSINESS ADDRESS.

A. My name is Carlette L. Walker. My business address is 1426 Main Street, Columbia, South Carolina.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by SCANA Services, Inc. as Assistant Controller of SCANA Corporation's regulated subsidiaries, including South Carolina Electric and Gas Company (the "Company" or "SCE&G").

Q. PLEASE BRIEFLY DESCRIBE YOUR EDUCATIONAL AND BUSINESS BACKGROUND.

A. I am a 1981 Cum Laude graduate of the University of South Carolina where I received a Bachelor of Science Degree in Accounting. Following graduation, I worked for two years in public accounting and became licensed as a Certified Public Accountant in the State of South Carolina. In 1983, I joined SCE&G's Internal Audit Department. After four years in Internal Audit, I accepted an accounting supervisory position with South Carolina Pipeline Corporation ("SCPC"). In 1994 I was promoted to Manager of SCPC's accounting department and in 1997 I was promoted to the position of Controller for that Company. In 1998 I accepted the position of SCE&G's Assistant Controller - Electric Generation and in 1999 was promoted to Assistant Controller - SCE&G. Effective in 2002, my responsibilities as Assistant Controller were increased to include all SCANA regulated subsidiaries. I am currently a member of the American Institute of Certified Public Accountants and the South Carolina Association of Certified Public Accountants.

Q. HAVE YOU PREVIOUSLY OFFERED TESTIMONY IN REGULATORY PROCEEDINGS?

A. Yes. I have testified before the Public Service Commission of South Carolina (the "Commission") in several past proceedings.

Q. PLEASE DESCRIBE THE SCOPE OF THE TESTIMONY YOU ARE PRESENTING.

A. In connection with Docket No. 2004-178-E and the Company's Application for Increases in Electric Rates and Charges ("the Application"), the Company provided certain exhibits containing financial information. I will discuss a number of the exhibits included in the Application (Exhibits D-I, D-II, D-IV, D-V) and certain other accounting and financial information.

Q. HOW ARE THE BOOKS AND RECORDS OF THE COMPANY MAINTAINED?

A. The books and records of the Company are maintained in accordance with generally accepted accounting principles and the Uniform System of Accounts for major utilities as prescribed by the Federal Energy Regulatory Commission ("the FERC"). This Uniform System of Accounts has been adopted by the Commission and is followed by major utilities subject to its jurisdiction. Compliance with generally accepted accounting principles and the Uniform System of Accounts is necessary in order to provide consistent and pertinent financial information to the general public, investors, regulators and the financial community.

Q. WHAT STEPS DOES THE COMPANY TAKE TO ENSURE THAT ITS BOOKS AND RECORDS ARE ACCURATE AND COMPLETE?

A. The Company maintains and relies upon an extensive system of internal accounting controls, audits by both internal and external auditors, and financial oversight by the Audit Committee of SCANA Corporation's Board of Directors. The Company's system of internal accounting controls is designed to provide reasonable assurance that transactions are properly recorded in the books and records and that assets are protected against loss or unauthorized use. The Company's system of internal accounting controls is evaluated annually by its independent auditors, Deloitte & Touche LLP, in connection with their audit. As a result of their latest audit, the independent auditors found no material weaknesses in the Company's system of internal accounting controls.

Q. WILL YOU PLEASE DESCRIBE EXHIBIT NO. ____ (EXHIBIT D-I OF THE APPLICATION)?

A. Exhibit No. ____ (D-I) consists of 7 pages and includes the Consolidated Balance Sheet for South Carolina Electric and Gas Company as of March 31, 2004, and the Consolidated Statement of Income for the twelve months ended March 31, 2004. These Statements were prepared in accordance with accounting principles applicable to regulated utilities and are consistent with similar statements previously filed with this Commission.

Q. WILL YOU PLEASE DESCRIBE EXHIBIT NO.____ (EXHIBIT CLW -1, APPLICATION D-II, PAGE 1 OF 3 OF THE APPLICATION)?

A. Exhibit No.___ (CLW -1, Application Exhibit D-II, page 1 of 3) is an analysis of the Company's electric operations that identifies operating revenues and expenses, income for return, original cost rate base, and rate of return for the twelve months ended March 31, 2004 (the "test year").

- **Column 1** provides a description of the items included in determining income for return and original cost rate base.
- **Column 2** presents the per books amounts used to determine income for return and original cost rate base for the test year.
- **Column 3** summarizes the Company's accounting and pro forma adjustments that are necessary to reflect known and measurable changes to the results of the Company's electric operations for the test year. The detail for each pro forma adjustment, by line, item is included in Exhibit No. _ (CLW -1, Application Exhibit D-II, page 3 of 3).
- **Column 4** presents the results of the Company's electric operations as adjusted for accounting and pro forma adjustments.

Q. WOULD YOU PLEASE EXPLAIN THE DERIVATION OF THE RATE OF RETURN ON ORIGINAL COST RATE BASE THAT APPEARS ON EXHIBIT NO. ___ (CLW -1, APPLICATION EXHIBIT D-II, PAGE 1 OF 3)?

A. Yes. If you take the total income for return on line 12 and divide it by the total original cost rate base as reflected on line 22, the result of this calculation is the rate of return on original cost rate base as reflected on line 23.

Q. WILL YOU PLEASE DESCRIBE EXHIBIT NO.____ (CLW-2, APPLICATION EXHIBIT D-IV)?

A. Exhibit No. ___ (CLW -2, Application Exhibit D-IV) is a Statement of Fixed Assets - Electric at March 31, 2004. This statement details gross Plant in Service and Construction Work in Progress ("CWIP") by FERC functional classification.

- **Column 1** sets out the FERC functional classifications.
- **Column 2** includes the amounts recorded on the books and records of the Company at March 31, 2004.
- **Column 3** summarizes the accounting and pro forma adjustments that affect Plant in Service and CWIP as detailed in Exhibit No. ____ (CLW-1, Application Exhibit D-II, page 3 of 3).
- **Column 4** shows the balances after including the effects of the adjustments identified in Column 3.

- **Column 5** contains the amount of adjusted gross Plant in Service and CWIP allocated to retail operations.

Q. WILL YOU PLEASE DESCRIBE EXHIBIT NO. ____ (CLW-3, APPLICATION EXHIBIT D-V)?

A. Exhibit No. _____ (CLW -3, Application Exhibit D-V) consists of two sections:

<u>Section One</u> --The first section is the Company's Statement of Depreciation Reserves for Electric Operations at March 31, 2004.

- **Column 1** sets forth the FERC functional classifications.
- **Column 2** shows the amounts recorded on the Company's books for the Reserve for Depreciation by FERC functional classification.
- **Column 3** summarizes the adjustments to Depreciation Reserves as detailed in Exhibit No.____ (CLW-1, Application Exhibit D-II, page 3 of 3.
- **Column 4** shows the balances after including the effects of the adjustments identified in column 3.
- **Column 5** is the amount of Depreciation Reserves allocated to retail operations.

<u>Section 2</u> --The second section is a Schedule of Annual Depreciation Rates for Electric Operations detailed by FERC functional classification.

- **Column 1** sets forth the FERC functional classifications.

- **Column 2** represents the rates that currently apply to the FERC functional classifications.

The column labeled "Requested" represents the composite depreciation rates that the Company is proposing based on a recently completed depreciation study.

Q. WILL YOU PLEASE DESCRIBE EXHIBIT NO.____ (CLW-1, Application **EXHIBIT D-II, PAGE 3 OF 3)?**

A. Exhibit No. ____ (CLW-1, Application Exhibit D-II, page 3 of 3) details the accounting and pro forma adjustments that the Company is proposing in this proceeding by the component of income and rate base to which each adjustment relates.

Q. PLEASE LIST THE ACCOUNTING AND PRO FORMA ADJUSTMENTS THAT YOU INTEND TO DISCUSS IN YOUR TESTIMONY.

A. The accounting and pro forma adjustments that I will be discussing are as follows. (The adjustment numbers coincide with the numbers on Exhibit No. ____ (CLW-1, Application Exhibit D, page 3 of 3.)

No.	Adjustment Title	Page
1.	Annualize NCEMC Contracts	9
2.	Amortize Unrecovered Fuel Component of Purchased Power	10

3.	Eliminate Short Term Capacity Purchases	10
4.	Update Williams Station Environmental Costs	10
5.	Annualize Turbine Maintenance O&M	11
6.	Selective Catalytic Reactor O&M	12
7.	Annualize Wages, Benefits and Payroll Taxes	12
8.	Pension and Health Care Related Adjustments	12
9.	Adjust Long-Term Disability Amortization	13
10.	Eliminate Demand Side Management Costs	14
11.	Eliminate Employee Clubs Investment and Expense	14
12.	Recognize Property Retirements	14
13.	Recognize Property Additions	15
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16.	Adjust Property Taxes	17
17.	Jasper Generation Project Adjustments	17
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19.	Adjust Fossil Fuel Inventory	20
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Q. PLEASE DESCRIBE THE ADJUSTMENTS.

A. **Adjustment No. 1, Annualize NCEMC Contracts,** annualizes the revenues associated with two contracts for sale of capacity and energy by SCE&G to the North Carolina Electric Membership Corporation. These sales are made under two separate contracts, one for 100 MW for a term of 2 years and one for 250 MW for a term of 9 years. Both contracts involve sales of capacity and energy from SCE&G's general system supply and went into force during January of 2004. The effect of this adjustment is to increase test year non-fuel revenue by $30,099,357.

Adjustment No. 2, Amortize Unrecovered Fuel Component of Purchased Power, adjusts expenses to amortize over three years the fuel component of purchased power that has not been recovered through the fuel adjustment clause in accordance with the stipulation approved by the Commission in Docket No. 2004-02-E. This adjustment increases test year expenses related to purchased power by $8,539,354.

. **Adjustment No. 3, Eliminate Short Term Capacity Purchases,** decreases test year operating expenses by $2,041,667 related to short term contracts for the purchase of capacity during the test year. These capacity purchases enabled the Company to maintain adequate reserve margins during the test year, but this capacity is no longer necessary now that the Jasper County Generating Station has begun commercial operation. Accordingly, the Company is removing the costs related to these contracts from its test year expenses.

<u>Adjustment No. 4, Update Williams Station Environmental Costs,</u> increases the level of test period expenses to reflect the annualized level of depreciation expense related to selective catalytic reactors installed at Williams Station after the close of the test period. The capital cost of these selective catalytic reactors is $74 million.

Williams Station is owned by South Carolina Generating Company ("GENCO") which is a wholly owned subsidiary of SCANA. SCE&G purchases all of the electric generation from Williams Station under a FERC approved formula rate that allows GENCO to recover capital costs and expenses. This adjustment increases test year expenses by $1,957,523.

<u>Adjustment No. 5, Annualize Turbine Maintenance O&M,</u> adjusts O&M expense for turbine maintenance costs as part of a proposed mechanism to levelize these costs over the 8 year maintenance cycle that applies to such turbines. The purpose of the proposed adjustment is to properly match maintenance expense with the year by year use of the plants that cause such expense to be incurred. Such adjustments are part of the Commission's long-standing process of "annualizing such [extraordinary] items to reflect more accurately their annual impact" as is required by existing Commission practice in setting test year expenses, (Order No. 2003-38, dated January 31, 2003, at p. 9).

To ensure that there is a matching of revenues and expenses, the Company will compare the actual costs incurred for turbine maintenance O&M each year to the expense level allowed in this case, and book any over or under-collections to regulatory asset or liability accounts subject to further orders of the Commission. The effect of this adjustment is to increase SCE&G's expenses by $5,412,193.

Adjustment No. 6, Selective Catalytic Reactor O&M, increases O&M expenses for costs associated with the use of ammonia in three new Selective Catalytic Reactor units installed at Wateree and Williams Stations. This equipment has been required by State and Federal air quality regulation to reduce NOx emissions at those plants. One of these units was placed in service during the test period, and the other two after the test year closed. The adjustment reflects annualized O&M expense related to the operation of this equipment. The effect of this adjustment is to increase test year expenses by $1,523,968.

Adjustment No. 7, Annualize Wages, Benefits and Payroll Taxes, annualizes the Company's salary expense at the end of the test year based on salary levels in effect in March of 2004. Corresponding adjustments have been made in payroll taxes and certain employee benefit costs. The effect of this annualization is to increase SCE&G's O & M expenses by $6,511,153 and taxes other than income taxes by $461,805.

<u>Adjustment No. 8, Pension and Health Care Related Adjustments</u>, reflects three adjustments related to benefits the Company provides its employees.

- **Pension Income --**This adjustment reduces O & M expenses by $3,688,534 to reflect an increase in the income derived from the Company’s pension plan during 2004 based on actuarial analysis. The performance of the Company’s pension fund has improved such that projected results for calendar year 2004 exceed the results for 2003, thereby enabling the Company to recognize an additional reduction in expense. This adjustment annualizes the effect of the additional income generated by the plan and reduces test year expenses by $3,688,534.
- **OPEBs --**This adjustment annualizes the electric O&M portion of the Company’s expenses for Other Post Employment Benefits (“OPEB”s), principally post-retirement health care benefits, to match the amounts required to be accrued for these future expenses under the Company’s actuarial study. The result is to increase test year O & M expenses by $1,342,303. In addition, this adjustment in OPEB expense requires a related reduction in rate base. The effect of this adjustment is to increase other deferred credits by $828,872.
- **Health Care --**This adjustment annualizes the increased cost of employee health care benefit expense in the first quarter of 2004 as compared to the test year. The effect of this adjustment is to increase expenses by $1,043,702.

<u>Adjustment No. 9, Adjust Long-term Disability Amortization,</u> increases expense for the amortization of deferred costs associated with the Company's long-term disability plan. In compliance with Statement of Financial Accounting Standards No. 112, the Company has accrued an $8.3 million liability associated with its long-term disability program. The Company has deferred these costs in a regulatory asset account and proposes to amortize them over 5 years. The effect of this adjustment is to increase expenses by $1,656,094.

Adjustment No. 10, Eliminate Demand Side Management Costs, reduces amortization expense for amounts associated with deferred Demand Side Management ("DSM") costs which were written off in June 2004. The effect of this adjustment is to decrease O&M expense by $508,601.

Adjustment No. 11, Eliminate Employee Clubs Investment and Expenses, reflects the removal of costs related to Employee Clubs (the Pine Island, Sand Dunes and Misty Lake Clubs) operated by the Company. The effect of the adjustment is to lower SCE&G's O&M expenses by $395,959, plant in service by $3,118,924, depreciation reserves by $1,063,885 and depreciation expense by $142,003. The Company is making this adjustment to comply with the Commission's established practice as set forth in past orders. By making this adjustment, the Company does not mean to imply that it agrees with this treatment of employee club expenses or that it may not object to removal of such costs from utility expenses in future proceedings.

Adjustment No. 12, Recognize Property Retirements, reduces the balance in the Company's Plant in Service Account by $13,497,257 to reflect pending retirements as of March 31, 2004. This adjustment is paired with a corresponding reduction in depreciation reserves.

<u>Adjustment No. 13, Recognize Property Additions</u>, updates the balance in the Company's Plant in Service Account and depreciation reserves to reflect other property additions and associated retirements.

- **Additional Plant Closings --**This adjustment increases plant in service by $79,417,726 and decreases CWIP by $77,062,203 related to certain other additions to property made as of May 31, 2004 but not accounted for in other pro forma adjustments.
- **Additional Retirements --**A related reduction is made to adjust depreciation reserves in the amount of $4,135,789 to reflect retirements related to these additions.
- **New NERC Standards --**This adjustment increases Plant in Service and O&M Expense for costs associated with compliance with new NERC standards related to increasing electric system reliability. These standards were adopted in response to the black-out affecting the midwestern and northeastern states during the summer of 2003. This adjustment increases plant in service by $1,309,000 ($240,000 of which is computer software to be amortized over 5 years), increases O&M expenses by $1,050,000, and increases amortization expense by $48,000.

<u>Adjustment No. 14, Annualize Current Depreciation Rates</u>, adjusts depreciation expense using the rates approved in Docket No. 95-1000-E and based on the adjusted plant in service balances. Consistent with prior Commission orders, including Order 96-15, the adjustment also considers the effect on the depreciation reserves consistent with the Commission's policy of crediting a full year of additional depreciation expense to depreciation reserves when rates are changed. The effect of this adjustment is to increase both annual depreciation expense and depreciation reserves by $7,559,637.

Adjustment No. 15, New Depreciation Study, reflects an increase in annual depreciation expense of $12,288,078 and a corresponding increase in depreciation reserves that results from the use of proposed depreciation rates derived from a recently completed depreciation study. See Exhibit No. _____ (JJS -1).

Q. IS THE COMPANY ASKING THAT THE NEW DEPRECIATION RATES BE APPROVED IN THIS PROCEEDING?

A. Yes. The Company is asking that the Commission approve in this proceeding new composite depreciation rates as shown in Exhibit D-V of the Application under the column labeled "Requested" and as supported by the depreciation study in Exhibit No. ____ (JJS -1) to the testimony of the Company's expert witness Mr. John J. Spanos. The Company also proposes to record depreciation expense going forward based on the rates associated with individual plant accounts as set forth in the depreciation study.

Q. PLEASE DISCUSS THE DERIVATION OF THE NEW ELECTRIC DEPRECIATION RATES.

A. The Company periodically reviews the adequacy of its depreciation rates for plant and equipment. These reviews, or depreciation studies, consider the productive life, cost of removal, salvage value and the mortality experience of the Company's property and equipment. As Mr. Spanos testifies, the rates reflected in the study being submitted to the Commission are derived to reflect a reasonable recovery period of the Company's capital investment.

Adjustment No. 16, Adjust Property Taxes, increases taxes other than income by $5,501,440. This adjustment is necessary to annualize the impact on the Company's property taxes by applying the current average millage rate to the additions to plant in service identified above.

Adjustment No. 17, Jasper Generation Project Adjustments, relates to the Jasper County Generation Project having been placed in service on May 1, 2004. This adjustment updates Plant in Service, Depreciation Expense, O&M Expenses (including firm capacity charges) and Property Taxes due to the addition of the Jasper Plant. There are four pro forma adjustments related to the plant:

- Plant in Service Adjustment places into Plant in Service the total amount of the Company’s investment in the Jasper Plant as of May 31, 2004 which is $506,039,714. It also removes $501,599,418 related to the plant from CWIP accounts.

- Depreciation and Property Taxes Expense Adjustment adjusts depreciation expenses and property taxes to reflect the plant having been placed in service. The depreciation adjustment is based on a depreciation rate of 4.0% as determined in the depreciation study presented by Company Witness Mr. Spanos by review of the estimated useful lives of the plant's major components and experience at the Company's other units. The amount of the depreciation adjustment is $20,130,017. Additional property taxes were calculated using the rates provided for in the negotiated fee in lieu of taxes agreement related to the plant. The amount of the additional property taxes is $5,182,359.
- O&M Expense Adjustment recognizes the O&M expense for the new gas-fired turbines and related assets. This O&M expense, on an annual basis, is $6,472,938.
- Fixed Pipeline Capacity Charges Adjustment reflects the removal of these charges from the fuel adjustment clause to allow recovery through base rates. The amount of the fixed pipeline capacity charges SCE&G must pay for the provision of interstate gas service to the Jasper facility is $15,292,800 per year. These charges are presently included in the Company's annual fuel forecast and are currently being recovered through the fuel adjustment clause. The Company is proposing to remove the retail portion of this amount ($10,922,000) from fuel adjustment clause calculations and include them in calculating base rates. In the initial period rates are in effect, this would reduce

the fuel factor computed in Docket No. 2004-02-E by $0.00057/kwh. To ensure that there is no over or under recovery of these charges in future years, the Company proposes to flow any positive or negative difference between the amount reflected in base rates and the actual charges for the fixed capacity charges through the fuel adjustment clause.

Q. WHAT IS THE RATIONALE FOR THIS PROPOSAL CONCERNING THESE FIXED CAPACITY CHARGES?

A. Because these charges do not vary with consumption of natural gas by the plant, we believe that it is proper to treat them as fixed costs. The Company's proposal allows a base amount of these capacity charges to be treated as fixed charges and allows any changes in the amount that may occur in the future to be treated as a variable charge through the fuel adjustment clause. This is consistent with the treatment the Commission authorized in Order No. 2003-38 related to the fixed capacity charges associated with the repowered Urquhart gas fired units.

<u>Adjustment No. 18, Saluda Dam Remediation Project</u>, removes from CWIP all amounts related to the project to remediate the Saluda Dam (the "Dam Remediation Project") for treatment according to the proposal set forth in the testimony of Company Witness Addison. The effect of this adjustment is to reduce the amount of the CWIP on the books as of March 31, 2004 by $193,091,618.

Adjustment No. 19, Adjust Fossil Fuel Inventory, increases the value of coal inventory to reflect current market prices and normal inventory levels, as discussed by Company Witness Lorick. The effect of the adjustment, reflecting both current prices and normalized inventory levels, is to increase rate base by $23,339,940.

Adjustment No. 20, Amortize GridSouth RTO Costs, reflects amortization of the Company's investment in the project to form GridSouth Regional Transmission Organization ("RTO"). The Company participated with Duke Power and Carolina Power and Light Company in this project, which was undertaken in response to directives issued by the FERC in Order 2000. The Company's investment in the project is $14,095,964 as of March 31, 2004 including carrying costs as permitted by FERC order. The Company is proposing to amortize this investment over 5 years with a resulting increase in annual O&M expense of $2,819,193. The Company has included in rate base $7,047,982 representing the average amount of investment which will be reflected on the Company's books during the five year amortization period requested.

Adjustment No. 21, Adjust Working Cash, adjusts working cash to reflect the working cash requirements related to the adjustments set forth above. The amount of the adjustment is an increase to rate base of $4,699,000.

Adjustment No. 22, Tax Effect of Annualized Interest, reflects the increases in State income taxes of $294,262 and Federal income taxes of

$1,956,842 associated with the pro forma adjustments to rate base discussed herein.

Q. MRS. WALKER, DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.